CREDIT UNION DIVISION

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AUTHORITY

The Credit Union Division is responsible for the regulation and supervision of state-chartered credit unions under the authority of the 1925 Public Act No. 285, as amended (The Michigan Credit Union Act). The division's primary goal is to ensure that state-chartered credit unions operate safely, soundly, and in compliance with applicable law.

PERSONNEL AND TRAINING

Director Roger Little has a highly trained, professional staff of examiners and office employees to fulfill the division's responsibilities. Assistant Director Paul Tautkus oversees corporate activities, Year 2000 supervision, and the Automated Systems Unit. Assistant Director Tim Standfest oversees the Examinations Unit with a staff of five Regional Supervisors, and 26 field examiners.

FIB management is strongly committed to providing training and development opportunities to its employees. Accordingly, division management and staff attended various professional development and refresher classes throughout 1998. The National Credit Union Administration (NCUA) and National Association of State Credit Union Supervisors (NASCUS) sponsored many of the classes which included the following: Year 2000 (Y2K) Compliance, Contemporary Critical Issues, Advanced Investments, Assessing Emerging Risks, Consumer Compliance, Senior Updates, Supervisory Committee Review and Fraud Detection, Problem Resolution, and Effective Writing.

The division also held a week-long training conference for its employees at Mt. Pleasant in June 1998. Several speakers led sessions on topics such as electronic banking, bond coverage, smart cards, risk-based examinations, consumer compliance, and Y2K issues.

In June 1998, Director Roger Little completed the final year of a three year program at the Graduate Banking School at Louisiana State University.

In November 1998, Senior Examiner Toni Girolami passed the CPA examination. Toni joins six other staff members that previously passed the CPA examination.

The division is accredited by NASCUS. Michigan was the first state to receive their accredited status on October 9, 1989. The division was re-accredited during 1994. The NASCUS re-accreditation is valid for a five-year period, subject to annual evaluation update reports. The division will undergo a re-accreditation review during 1999.

EXAMINATION AND SUPERVISION

The division met its regulatory and supervisory responsibilities in 1998 by conducting an annual examination at each of the 316 (including CenCorp) state-chartered credit unions. The division also performed 45 follow-up examinations at 39 credit unions that exhibited problem areas at the annual examination or through off-site monitoring.

The division manages its resources using "risk-focused supervision." The division accomplishes this by continuously assessing each credit union, and scheduling examinations and setting examination scopes based on identified risks.

Each state-chartered credit union is assigned to an Examiner in Charge (EIC). Each EIC is responsible for the ongoing monitoring of the overall performance and condition of assigned institutions. Early warning statistical reports, developed by Examination Manager Scott Thompson, also help alert the division to emerging problems.

The division sends a Pre-Examination Inquiry to credit unions prior to each examination. Using the information provided, the EIC's target risk areas, and set a preliminary examination scope prior to each on-site examination.

The division continued monitoring each credit unions' progress with Y2K compliance. On May 4, the division sent a letter to each credit union board of directors containing specific actions to achieve Y2K compliance and milestone dates. Examiners evaluated credit unions' Y2K compliance status at each examination in 1998. The division collected quarterly Y2K status reports from each credit union in 1998 on behalf of NCUA. The division also performed Y2K specific examinations at 11 selected credit unions and 13 independent service vendors. The division entered into Memorandums of Agreement with seven credit union boards of directors due to their failure to progress satisfactorily with ensuring Y2K compliance; they have since made improvements. Overall, state-chartered credit unions and their independent service providers appear to be progressing satisfactorily with Y2K compliance.

Meeting with credit union representatives to discuss examination issues is an integral component of the division's supervision function. Division representatives meet with key management personnel at the conclusion of every examination. Division representatives also met with boards of directors at 48 of the 316 state-chartered credit unions to discuss examination issues in 1998.

We continue to work cooperatively with our federal counterpart, the NCUA. FIB examinations and NCUA insurance reviews are performed jointly at selected credit unions. Division representatives meet regularly with NCUA representatives for planning purposes and to discuss emerging issues.

While the economy remained strong in 1998, and the overall condition of credit unions remained favorable, some individual credit unions suffered with poor earnings, high delinquency, high loan losses, and reduced capital. These conditions and other identified risks were typically the result of poor management, and decisions made without adequate research and planning.

To address these managerial weaknesses, the division issued Credit Union Bulletin 98-1 on December 9, 1998. The purpose of the bulletin was to clarify the Bureau's position on the duties and responsibilities of credit union directors. Each board of directors must develop a Directorship Policy that sets requirements and guidelines for directors, and clearly states the board's view of its role in guiding the credit union.

The number of credit unions with CAMEL 3, 4, or 5 ratings declined 19% in 1998. Of the 316 credit unions supervised, the division assigned CAMEL ratings of 3 or lower to 35, representing 10% of total credit union assets.

CORPORATE CHANGES

Of the 499 credit unions in Michigan, 316, or 63%, are state-chartered — down from 321 at year-end 1997. During 1998, five credit unions merged into other state-chartered credit unions; one credit union merged into a federally-chartered credit union; and one credit union converted from a federal to a state charter. The most common reasons for the mergers were to realize economies of scale, and to provide more services to the members of the merging credit union.

Bylaw amendments continued at a strong pace in 1998. Besides field of membership amendments, the most common bylaw amendment was to Article XII, which governs lending. Many credit unions converted to the less-restrictive Article XII, Option 1 language. One credit union re-wrote their entire bylaws to streamline and remove redundancies.

Field of membership changes slowed from recent years past. Of the 316 state-chartered credit unions, the Bureau has approved 144 to serve multiple groups as provided in Section 5 of the Michigan Credit Union Act, and the Addendum to Credit Union Policy Bulletin 83-1. The Bureau authorized all but 11 of these fields of membership prior to 1998.

The division processed 10 corporate name change requests in 1998, generally to more accurately represent the credit unions' expanded fields of membership.

FEDERAL LEGISLATION

On February 25, 1998, the United States Supreme Court ruled that NCUA's longstanding select employee group policy was contrary to the plain language of the field of membership provisions of the Federal Credit Union Act. The court's ruling did not, however, directly affect state-chartered credit unions and their fields of membership.

On August 7, 1998, President Bill Clinton signed into law the Credit Union Membership Access Act of 1998, HR 1151. The Act explicitly authorizes multiple group chartering for *federal* credit unions, and makes other changes in the Federal Credit Union Act; some of which affect *all federally-insured* credit unions. For Michigan state-chartered credit unions, the act primarily:

1. Imposes a new aggregate limit on a credit union's outstanding member business loans; and
2. Establishes a system of tiered capital requirements taking effect August 7, 2000. For credit unions not meeting the standard, progressively more stringent "prompt corrective action" requirements will apply.

FINANCIAL TRENDS

Michigan state-chartered credit unions experienced 12% asset growth in 1998 — the strongest since 1986. Less than 40% of the asset growth was converted to loans; over 60% flowed into credit union investment portfolios. As a result, the aggregate Loans to Assets Ratio declined from 64% at year-end 1997 to 61% at year-end 1998. Aggregate investments grew 25% in 1998 with 54% of the growth flowing into corporate credit unions, and 43% into the "other investment" category consisting primarily of corporate obligations. The aggregate return on assets declined slightly in 1998, but remained strong at .97%. Overall, credit unions remained well capitalized at 11.46% of assets.

INDUSTRY ASSOCIATIONS

Division management remains committed to working cooperatively with trade associations and other professional organizations for the overall benefit of the credit union industry. Accordingly, division personnel attended numerous industry-related functions in 1998. Staff members also presented various topics in 1998 for the Michigan Association of Credit Unions, the Michigan Credit Union League, the Michigan Association of CPA's, and the MSU Office of Urban Affairs.

The division remains closely involved with NASCUS at the national level. NASCUS is dedicated to the promotion of the dual chartering system and the advancement of the autonomy and expertise of state credit union regulatory agencies. Director Roger Little serves on the Regulatory Development Committee which designs, monitors, and implements programs which strengthen state credit union supervisory agencies. The most significant product of this committee in 1998 was the creation of a viable cooperative supervisory agreement for the monitoring of multi-state credit unions. The agreement was endorsed by every state supervisory agency. Among many other projects, the committee is also commissioning an intensive study of all NCUA rules and regulations affecting state-chartered credit unions.

Semi-annually, an advisory council of credit unions meets with the Commissioner of the Bureau and other senior staff to discuss and advise on current issues and topics that face credit unions. The council is made up of 15 credit union managers and a volunteer credit union board member representing a variety of credit unions from around the state. Some of the issues discussed in 1998 were director qualifications, HR 1151, field of membership, ATM surcharges, ATM fraud, interstate branching, Y2K, industry trends, member business loan rules, and merger policies.

LOOKING FORWARD

In 1999, the division will continue to provide a high-quality examination and supervision program. The division's "risk-focused supervision" will enable a proper allocation of resources and attention to the most critical issues.

The division is currently developing a comprehensive internal data base which will contain current and historic data on each credit union. Staff members will have easy access to credit union data to aid in their supervision responsibilities. Staff members will also be able to respond more rapidly to requests for data.

The division will continue to closely monitor credit unions' efforts toward Y2K compliance. Credit unions must complete Y2K testing by June 30, 1999, and should also have established contingency and liquidity plans.

Y2K compliance and meeting members' needs in an ever-changing competitive market should be top priorities of each credit union board of directors.

Visit us at our web page at http://www.cis.state.mi.us/fib/. The web site contains credit union listings (by name and by city), statutes, rules, bylaws, bulletins, forms, applications, Y2K plans and resources, and answers to frequently asked questions.

Consolidated Balance Sheet of State-Chartered Credit Unions

(EXCLUDES CENTRAL CORPORATE CREDIT UNION) (IN THOUSANDS)

	December 31, 1998	December 31, 1997	Percent Increase (Decrease)
ASSETS			
Loans			
Unsecured/Credit Card/Lines of Credit	$ 1,302,690	$ 1,329,341	(2.00) %
Vehicle	2,680,686	2,638,316	1.61
Real Estate	2,824,129	2,332,319	21.09
Other	581,058	584,838	(.65)
Allowance for Loan Losses	(57,128)	(56,096)	1.84
Investments			
U.S. Government Obligations and Federal Agency Securities	663,662	705,753	(5.96)
Corporate Credit Unions	1,454,248	1,024,329	41.97
Other Credit Unions	18,427	15,320	20.28
Commercial Banks, Savings and Loans, and Mutual Savings Banks	544,950	476,327	14.41
Mutual Funds and Common Trust Investments	45,768	35,361	29.43
NCUA Share Insurance Capitalization Deposit	90,871	85,109	6.77
Other	1,240,451	1,001,463	23.86
Cash and Cash Equivalents	301,881	260,755	15.77
Net Fixed Assets	260,894	231,362	12.76
Other Assets	146,794	130,811	12.22
Total Assets	$12,099,381	$10,795,308	12.08%
LIABILITIES AND EQUITY			
Liabilities			
Notes Payable	$ 39,125	$ 31,025	26.11 %
Accrued Dividends/Interest Payable	31,453	33,808	(6.97)
Other Liabilities	75,660	75,215	.59
Savings			
Regular Shares	3,779,604	3,563,651	6.06
Share Drafts	1,319,045	1,088,862	21.14
Money Market Shares	1,853,884	1,540,728	20.33
Share Certificates	2,297,391	1,944,301	18.16
IRA/KEOGH	864,234	832,491	3.81
Other	452,458	418,584	8.09
Equity			
Regular Reserves	394,569	363,970	8.41
Investment Valuation Reserve	559	887	(36.98)
Accumulated Unrealized Gains (Losses) on Available for Sale Securities	30,625	23,758	28.90
Other Reserves	207,262	198,240	4.55
Undivided Earnings	753,512	679,788	10.85
Total Liabilities and Equity	$12,099,381	$10,795,308	12.08 %

Consolidated Statement of Operations of State-Chartered Credit Unions

(EXCLUDES CENTRAL CORPORATE CREDIT UNION) (IN THOUSANDS)

	December 31, 1998	December 31, 1997	Percent Increase (Decrease)
Operating Income			
Interest on Loans	$639,101	$603,822	5.84 %
Less: Interest Refunded	(3,225)	(3,903)	(17.37)
Income from Investments	220,876	203,017	8.80
Fee Income	66,481	60,076	10.66
Other Operating Income	22,638	18,676	21.21
Total Operating Income	945,871	881,688	7.28
Cost of Funds			
Dividends	174,173	171,795	1.38
Interest on Deposits	212,702	183,416	15.97
Interest on Borrowings	1,772	1,983	(10.64)
Total Cost of Funds	388,647	357,194	8.81
Net Margin	557,224	524,494	6.24
Operating Expenses			
Employee Compensation and Benefits	192,497	177,965	8.17
Cost of Space	27,572	24,735	11.47
Office Operations Expense	94,730	88,470	7.08
Professional and Outside Services	35,565	32,933	7.99
Operating Fees	4,284	4,122	3.78
Other Operating Expense	59,432	56,542	5.11
Provision for Loan Losses	34,663	30,366	14.15
Total Operating Expenses	448,743	415,133	8.10
Net Operating Income	108,481	109,361	(.80)
Non-Operating Gains	2,047	13	
Net Earnings	110,528	109,374	1.06 %

Significant Data and Financial Ratios of State-Chartered Credit Unions
(EXCLUDES CENTRAL CORPORATE CREDIT UNION)

SIGNIFICANT DATA

	1998	1997	1996	1995	1994
Number of credit unions	315	320	323	334	339
Number of credit union members	2,516,915	2,445,380	2,412,073	2,377,955	2,330,276
Total assets*	$ 12,099,381	$ 10,795,308	$ 10,021,691	$ 9,403,097	$ 8,958,894
Total loans outstanding*	7,388,563	6,884,814	6,269,436	5,716,202	5,207,925
Total shares and deposits*	10,566,616	9,388,617	8,765,771	8,259,599	7,933,034
Amount of loans granted during year*	4,214,076	3,769,350	3,536,764	3,100,613	3,188,527

* (in thousands)

SIGNIFICANT RATIOS

Net Equity/Total Assets	11.46%	11.73%	11.28%	10.78%	9.84%
Delinquent Loans/Total Loans	0.89	0.99	0.99	0.89	0.83
Allowance for Loan Losses/Delinquent Loans	87.24	82.37	87.76	104.44	125.06
Allowance for Loan Losses/Total Loans	0.77	0.81	0.87	0.93	1.03
Net Charge-Offs/Average Loans	0.47	0.45	0.37	0.30	0.28
Net Income/Average Assets	0.96	1.05	1.10	1.13	1.13
Gross Income/Average Assets	8.26	8.47	8.33	8.20	7.61
Cost of Funds/Average Assets	3.40	3.43	3.34	3.30	2.82
Net Margin/Average Assets	4.86	5.04	4.99	4.90	4.79
Operating Expenses(-PLL)/Average Assets	3.62	3.70	3.65	3.60	3.50
Provision for Loan Losses/Average Assets	0.30	0.29	0.24	0.17	0.16
Loan Income/Average Loans	8.96	9.18	9.28	9.29	9.16
Investment Income/Average Investments	5.97	6.18	5.89	5.70	4.89
Interest and Dividends/Average Total Savings	3.88	3.91	3.80	3.72	3.16
Total Loans/Total Assets	61.07	63.78	62.56	60.79	58.13
Total Investments/Total Assets	33.54	30.97	32.15	33.58	36.76
Fixed Assets/Total Assets	2.16	2.14	2.05	2.05	1.98
Total Loans/Total Savings	69.92	73.33	71.52	69.21	65.67
Total Borrowings/Total Savings	0.37	0.33	0.21	0.23	0.20

DISTRIBUTION OF GROSS INCOME

Interest refunded to borrowers	0.34%	0.44%	0.44%	0.48%	0.56%
Operating expense	43.63	43.45	43.60	43.87	46.02
Provision for loan loss expense	3.65	3.43	2.83	2.13	2.14
Interest on borrowings	0.19	0.22	0.11	0.14	0.10
Interest and dividend cost	40.76	40.11	39.83	40.23	37.00
Retained earnings	11.43	12.35	13.19	13.15	14.18
Total	100.00%	100.00%	100.00%	100.00%	100.00%

Classification of State-Chartered Credit Unions by Asset Size

(EXCLUDES CENTRAL CORPORATE CREDIT UNION)

	Number of Credit Unions 1997	Number of Credit Unions 1998	Increase (Decrease) In Number From Prior Year	1998 Total Assets (000's Omitted)	Percentage In Group
$250,000 or less	5	6	1	$ 915	0.01%
$250,000 to $500,000	10	6	(4)	2,575	0.02
$500,000 to $1,000,000	11	11	0	7,126	0.06
$1,000,000 to $2,000,000	23	21	(2)	29,447	0.24
$2,000,000 to $5,000,000	45	39	(6)	129,743	1.07
$5,000,000 to $10,000,000	46	43	(3)	299,183	2.47
$10,000,000 to $20,000,000	46	48	2	674,675	5.58
$20,000,000 to $50,000,000	82	78	(4)	2,680,621	22.15
$50,000,000 to $100,000,000	28	35	7	2,328,846	19.25
$100,000,000 to $200,000,000	14	17	3	2,251,178	18.61
$200,000,000 to $400,000,000	8	8	0	2,236,183	18.48
Over $400,000,000	2	3	1	1,458,889	12.06
Total	320	315	(5)	$12,099,381	100.00%

Credit Union Division Staff

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